

Message Text

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FM AMEMBASSY LONDON

TO SECSTATE WASHDC 9473

C O N F I D E N T I A L SECTION 01 OF 02 LONDON 04348

LIMDIS

PASS TREASURY AND FRB

E.O. 11652: XGDS-1

TAGS: EFIN, UK

SUBJECT: AMBASSADOR'S TOUR D'HORIZON WITH CHANCELLOR
HEALEY

SUMMARY: HEALEY GIVES EVERY INDICATION THE FORTHCOMING BUDGET WILL BE AT LEAST NEUTRAL, PERHAPS TOUGH, CERTAINLY RESPONSIBLE, TAKING INTO ACCOUNT NEED TO GIVE REASSURANCE TO THE INTERNATIONAL FINANCIAL COMMUNITY OF SOUNDNESS OF U.K. ECONOMY. THIS MUCH SAID, CHANCELLOR SEEMS CONCERNED THAT ON AVERAGE, BRITAIN'S RATE OF INFLATION THIS YEAR PROBABLY WILL BE TWICE THAT OF ITS MAJOR TRADING PARTNERS AND COULD SEE SITUATIONS IN WHICH SELECTIVE IMPORT CONTROLS MIGHT BE JUSTIFIED AS BEING THE LEAST HARMFUL ALTERNATIVE. END SUMMARY.

1. HEALEY BEGAN LUNCHEON CONVERSATION BY NOTING THAT HE HAD JUST WON A PERSONAL VICTORY OVER THE LEFT WING OF THE LABOUR PARTY. HE EXPLAINED THAT THE LEFT-WING TRIBUNE GROUP, BY A MAJORITY OF ROUGHLY 2 TO 1, HAD ENDORSED HIS ECONOMIC POLICIES. THEY WERE BEGINNING TO UNDERSTAND THE IMPORTANCE OF CONTROLLING INFLATION. HIS FORTHCOMING
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BUDGET WILL BE A VERY IMPORTANT ONE, SETTING THE TONE

AND DIRECTION OF THE BRITISH ECONOMY DURING THE NEXT THREE YEARS. HE HAS PRACTICALLY RULED OUT THE POSSIBILITY OF ANY REFLATION. OVER ONE BILLION POUNDS WAS INJECTED INTO U.K. ECONOMY IN 1974 BUDGETS; THAT STIMULATION WILL HAVE TO SUFFICE. DURING 1975 U.K. INFLATION WOULD BE ROUGHLY TWICE THE LEVEL IN THAT OF ITS MAJOR TRADING PARTNERS. THERE SHOULD BE SOME NOTICEABLE DECLINE IN THE RATE TOWARDS THE END OF THE YEAR, BUT UNTIL THEN THERE WAS TOO MUCH INFLATIONARY PRESSURE IN THE PIPELINE TO REASONABLY FORECAST ANY REDUCTION IN THE RATE.

2. HEALEY SAID THAT THE BUDGET WOULD BE IMPORTANT FOR ITS SHORT-TERM IMPLICATIONS AS WELL AS FOR ITS MEDIUM AND LONGER TERM IMPACT. FOREIGN LENDERS AND INVESTORS WILL BE WATCHING CAREFULLY. WHEREAS HE DIDN'T THINK IT WOULD BE NECESSARY FOR THE U.K. TO BORROW FROM THE IMF THIS YEAR, HE ADDED THAT HIS BUDGET WOULD PROBABLY BE SUCH AS TO MEET ANY CONDITIONS THE IMF MIGHT REQUIRE IF THE U.K. WERE TO CONSIDER A SIZEABLE DRAWING. CHANCELLOR STRESSED THE POLITICALLY SENSITIVE NATURE OF HIS REMARKS IN A PRE-BUDGET CONTEXT. WE ASSURED HIM THAT THEY WOULD BE HELD CLOSELY AND NOT COMPROMISED. HEALEY ALSO POINTED OUT THAT BUDGET PLANNING IS STILL IN THE FORMATIVE STAGE, NO FINAL DECISIONS TAKEN.

3. WE STRESSED THE IMPORTANCE OF AVOIDING IMPORT CONTROLS WHICH COULD LEAD TO AN INTERNATIONAL ROUND OF RETALIATION AND RECRIMINATION. THE CHANCELLOR SAID THERE IS CONSIDERABLE PRESSURE FROM THE TEXTILE AND AUTOMOBILE INDUSTRIES TO IMPOSE IMPORT CONTROLS. HE ADDED THAT THERE IS ALSO A RESPECTABLE SCHOOL OF INTELLECTUAL THOUGHT, INCLUDING THE TUC AND THE CAMBRIDGE ECONOMIC GROUP, WHICH ARGUES THAT SELECTIVE IMPORT CONTROLS ARE A LESSER EVIL THAN MORE GENERALIZED DOMESTIC DEFLATION OR DEVALUATION OF THE EXCHANGE RATE. THE CHANCELLOR RECOGNIZED THE VALIDITY OF THE ARGUMENTS AGAINST SELECTIVE IMPORT CONTROLS, BUT DURING THE DISCUSSION HE DID NOT SPECIFICALLY RULE OUT THE POSSIBILITY OF THEIR BEING INTRODUCED. ON THE OTHER SIDE OF THE COIN, HE SAW A MORE GENERAL NEED FOR THE MAJOR INDUSTRIALIZED COUNTRIES, SPECIFICALLY THE U.S., GERMANY AND

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JAPAN, TO REFLATE THEIR ECONOMIES IN ORDER TO REKINDLE THE GROWTH IN WORLD TRADE. IN THIS CONNECTION HE CITED RECENT DISCUSSIONS IN WP-3 AND EPC AND OF THE EC FINANCE MINISTERS. (TRADE MINISTER PETER SHORE ALSO HAS STRESSED IMPORTANCE OF REFLATION IN TRADE "SURPLUS" ECONOMIES IN RECENT CONVERSATIONS WITH EMBASSY OFFICERS; HE REMAINS NEGATIVE ON IMPORT CONTROLS.)

4. LOOKING AHEAD, THE CHANCELLOR INDICATED THAT SOME OF HIS OTHER MORE IMMEDIATE PROBLEMS CONCERN THE WAGE CLAIMS OF THE POWER WORKERS AND RAILWAY MEN. THE ECONOMY COULD NOT STAND A STRIKE BY THE POWER WORKERS, THE GOVERNMENT

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CANNOT RISK ONE, AND BOTH REALIZE THIS. ON THE OTHER HAND, THE GOVERNMENT MAY CONCLUDE THAT IT CAN WIN IF IT DECIDES TO REFUSE THE RAILWAYMEN'S DEMANDS, ALTHOUGH NO FIRM DECISION HAS YET BEEN TAKEN. THE PARAMOUNT CONSIDERATION, ACCORDING TO THE CHANCELLOR, IS NOT TO REPEAT THE MISTAKES OF THE HEATH GOVERNMENT IN WHICH THE GOVERNMENT ACCEPTED CONFRONTATIONS AND THEN LOST THE BATTLES AND THE WAR. HEALEY READILY ADMITTED THAT CLASS ANIMOSITIES HERE ARE THE SHARPEST IN EUROPE. HIS CURRENT WIDE-RANGING TAX PROPOSALS ARE AIMED AT REDUCING THE WIDEST ECONOMIC EXTREMES. HE REFLECTED PHILOSOPHICALLY, HOWEVER, THAT PERHAPS THE MEASURES WILL BE TOO SEVERE ON THE MIDDLE CLASSES WHICH ARE BEING PRESSED VERY HARD.

6. DURING DISCUSSION OF THE EC REFERENDUM, HEALEY ESTIMATED THAT PERHAPS THERE WOULD BE A 60 PERCENT TURNOUT AND THAT THE VOTE WOULD BE 55 TO 45 IN FAVOR OF REMAINING IN. HE ADVISED U.S. OFFICIALS AND THE U.S. GOVERNMENT NOT

TO BECOME INVOLVED IN THIS ISSUE, WHICH IS BASICALLY A
DOMESTIC ONE. THERE ARE STRONG, IF INCHOATE, FEELINGS ON
THE ISSUE OF U.K. SOVEREIGNTY. IF QUERIED, U.S. OFFICIALS
WOULD BE BEST ADVISED TO REPLY IT IS A MATTER THE U.K.
MUST DECIDE FOR ITSELF.

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